ESO 1883

ROLL-OVER HEDGE ANALYSIS

Corn Drought Years

Guidelines

and

Resource Materials

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I. During droughts, the spread between old and new crop contracts often becomes relatively large.

Example: '88 DROUGHT

July '89 Contract	@	$3.10
Dec. '89 Contract	@	2.40
SPREAD		$ .60

II. Expect spread to narrow to 10¢

A. Old crop ('88) price ↓

- Large new crop ('89)

B. New crop ('89) price ↑

- Small new crop ('89)

III. Outcome when old crop price ↓

A. Now (summer '88)

1. Sell old crop (July '89)	$ 3.10
2. Buy new crop (Dec. '89)	2.40

B. Future

3. Assume spread ↓	.10
4. Old crop price ↓	2.50
5. New crop price →	2.40
6. Buy old crop	2.50
Profit (3.10 - 2.50)	.60
7. Sell new crop	2.40
8. Hedge price	3.00
9. Worst case scenario	3.00

IV. Outcome when new crop price ↑

A. Now (summer '88)

1. Sell old crop (July '89)	$ 3.10
2. Buy new crop (Dec. '89)	2.40

B. Future

3. Assume spread ↓	.10
4. Old crop price →	3.10
5. New crop price ↑	3.00
6. Buy old crop	3.10
7. Sell new crop	3.00
Profit (3.00 - 2.40)	.60
8. Sell new crop	3.00
9. Best case scenario	3.60

ROLL-OVER HEDGE ANALYSIS
Corn Drought Years

(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)	(J)
		June-Sept. High Futures		July 1 Futures		Sept.-Nov. Low Futures		Profit@	
Crop Year	Date	July	Dec.	July	Dec.	Dec.	Date	Straight Hedge	July/Dec. Hedge
		($/bu.)	($/bu.)	($/bu.)	($/bu.)	($/bu.)		(D-G) ($/bu.)	(C-E+F-G) ($/bu.)
70-71#	9/15	1.68	1.52 (10/26)	1.52	1.46	1.12	10/01	.40	.50
74-75	9/30	3.99*	3.45	2.71	2.33	2.57	11/19	.88	1.04
80-81#	9/08	3.79	3.54 (9/22)	3.24	3.46	2.61	11/30	.93	1.40
83-84	8/25	3.88	3.25	3.51	3.11	2.64	11/30	.61	.84
88-89	6/23	3.53	2.86	2.72	2.61	2.18	8/03	.68	1.24
Average								.70	1.00

@ Before taxes, interest, and commissions
# Dec. not trading when July reached summer high (sold first day traded)
* Contract high $4.11 on 10/7/74